IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 5 of 1989

For Approval and Signature:

Hon'ble MR.JUSTICE A.R.DAVE
and
Hon'ble MR.JUSTICE D.A.MEHTA

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : NO

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the concerned Magistrate/Magistrates,Judge/Judges,Tribunal/Tribunals? : NO

COMMISSIONER OF INCOME-TAX

Versus

SAYAJI MILLS LTD.

Appearance:

1. INCOME TAX REFERENCE No. 5 of 1989
MR MANISH R BHATT for Petitioner No. 1
NOTICE SERVED for Respondent No. 1

CORAM : MR.JUSTICE A.R.DAVE
and
MR.JUSTICE D.A.MEHTA

Date of decision: 12/09/2002

ORAL JUDGEMENT

(Per : MR.JUSTICE A.R.DAVE)

At the instance of the Commissioner of Income-tax, the following questions of law, arising out of the order passed in I.T.A. No. 1556/Ahd/1985, have been referred to this Court for its opinion under the provisions of Section 256(1) of the Income-tax Act, 1961 (hereinafter referred to as the 'Act').

1. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal is right in law in granting deduction under section 35B on expenditure incurred by the assessee in connection with development of export market?

2. Whether, the Appellate Tribunal is right in law in holding that professional fees of Rs. 1 lacs was an expenditure of revenue nature and therefore deductible while computing total income?.

2. We have heard learned Standing Counsel for the Central Government Shri B.B. Naik for the applicant-revenue. Nobody has appeared for the respondent assessee, though the respondent assessee has been duly served with the notice of this Court.

3. So far as the first question is concerned, it has been submitted by the learned advocate appearing for the revenue that the said question has already been answered by this Court in the case of COMMISSIONER OF INCOME-TAX Vs. GIRDHARLAL VITHALDAS 196 I.T.R. 316. Looking to the law laid down by this Court in the said judgement, we answer the first question in the negative i.e. in favour of the revenue and against the assessee.

4. So far as the second question is concerned, it pertains to the nature of expenditure, which the respondent assessee had incurred by way of professional fees paid to the lawyers for the purpose of defending a suit filed against the respondent assessee. The facts and circumstances in which the said question has arisen are as under:

5. The respondent-Company had entered into an agreement to sell one of its units named Sayaji Mills No. 2 situated at Bombay with Punaloor Paper Mills Ltd. (hereinafter referred to as 'PPML'). By virtue of the agreement dated 22nd December, 1977, which the assessee had entered into with PPML, it was open to PPML to nominate someone in whose favour sale of Sayaji Mills No.

2 was to be effected. In pursuance of the agreement, PPML nominated Aradhana Investments Limited (hereinafter referred to as 'AIL') to purchase the property which was to be sold by the assessee.

6. It appeared to the respondent assessee that AIL was not having sufficient funds to make payment of the consideration which the assessee had to receive. AIL had initiated legal proceedings for the purpose of getting possession of the asset, which was sought to be sold by the assessee. A suit was filed by AIL for specific performance of the agreement, which the assessee had entered into with PPML. The said suit had to be resisted by the assessee so as to see that the assessee Company is not constrained to part with the possession of the property which was to be sold in pursuance of the agreement referred to hereinabove. The assessee had an apprehension that if possession of the property in question was given to AIL, possibly the assessee would not get the amount of consideration from AIL. In the circumstances, substantial amount had to be spent by the assessee for defending the suit which was filed by AIL against the assessee.

7. In the process of defending the suit, an expenditure to the tune of Rs. 1 lakh had been incurred by the assessee. The said amount of expenditure had been incurred towards professional fees and possibly that was paid to the concerned lawyers.

8. The amount of expenditure incurred by the assessee was not allowed by the Assessing Officer and, therefore, the assessee had filed an appeal against the order passed by the Assessing Officer. The CIT (Appeals) confirmed the order passed by the Assessing Officer in the Appeal. Being aggrieved by the order passed by the CIT (Appeals), the assessee had filed second appeal before the Appellate Tribunal. Relying upon the observations made by the Hon'ble Supreme Court in the case of EMPIRE JUTE CO. LTD. Vs. COMMISSIONER OF INCOME-TAX (1980) 124 I.T.R. 1, the Tribunal came to the conclusion that the expenditure incurred by the assessee towards professional fees was an allowable expenditure as it was an expenditure in the nature of revenue expenditure.

9. In the facts and circumstances of the case referred to hereinabove, this Court has to decide whether the amount of expenditure incurred in the nature of professional fees of Rs. 1 lakhs was rightly treated as revenue expenditure by the Tribunal.

10. For the purpose of answering the question, it is absolutely necessary to know the circumstances in which the assessee was constrained to incur the said expenditure in the nature of professional fees.

11. As stated hereinabove, property of the assessee was agreed to be sold under the agreement dated 22nd December, 1977 to PPML. As per the terms of the agreement to sell, PPML had nominated AIL to purchase the property. No consideration had passed either from PPML or from AIL to the respondent assessee and, therefore, possession of the property to be sold had not been given either to PPML or to AIL by the respondent assessee.

12. It appears that AIL was not financially sound and possibly was not in a position to pay the amount of consideration to the respondent assessee. As possession of the property in question had not been handed over to AIL, AIL filed a suit for possession or for specific performance of the agreement dated 22nd December, 1977 in West Bengal. The respondent assessee had to defend the said suit and for that purpose had to incur expenditure in the nature of professional fees paid to the lawyers. The said expenditure was not allowed by the Assessing Officer as he was of the view that the said expenditure was not revenue expenditure.

13. Looking to the facts recorded by the Tribunal, it is very clear that the assessee had to protect its property because if the suit had not been defended properly, the assessee would have been constrained to part with the possession of the property. Thus, for the purpose of protection of the property belonging to the respondent assessee, the assessee had incurred the expenditure, which it had claimed as revenue expenditure, allowable under the provisions of Section 37 of the Act.

14. It is not in dispute that the litigation had been initiated by AIL and as a defendant the respondent assessee had to defend the suit so as to protect its property.

15. Looking to the law laid down by the Hon'ble Supreme Court in the case of EMPIRE JUTE CO. LTD Vs. COMMISSIONER OF INCOME-TAX 124 I.T.R. 1, the Tribunal came to the conclusion that as the expenditure was incurred by the assessee for the purpose of preserving and maintaining its capital asset, the expenditure incurred by the assessee was allowable as revenue expenditure. The Tribunal also came to the conclusion

that the expenditure so incurred by the assessee had no connection with the acquisition of a capital asset because the expenditure of such a nature can be incurred only by the purchaser and in the instant case, the assessee was not a purchaser. It was also found by the Tribunal that the expenditure was not incurred for the purpose of curing any defect of the assessee's title in respect of the property, which was sought to be sold by the assessee. Looking to the facts referred to hereinabove, the Tribunal came to the conclusion that the expenditure was allowable as revenue expenditure.

16. We have gone through the record and have also heard the learned advocate appearing for the revenue. It has been argued by him that the expenditure was incurred by the assessee for getting the consideration from AIL. For the said reasons, according to the learned advocate, the expenditure which had been incurred cannot be said to be revenue expenditure. It has been submitted by him that the expenditure had been incurred for a litigation which was mainly for the purpose of getting consideration from AIL and thus, it had some relation with the capital asset of the respondent assessee. For the said reason, it has been submitted by him that the expenditure was rightly not allowed by the Assessing Officer and even the appeal filed against the order passed by the Assessing Officer was rightly dismissed by the C.I.T. (Appeals).

17. Looking to the facts of the case, in our opinion the submission made by the learned advocate is not correct. The litigation, which had been initiated by AIL, was for the purpose of getting possession of the property in question and for specific performance of the agreement dated 22nd December, 1977. By no stretch of imagination, it can be said that the expenditure was incurred for the purpose of getting consideration from AIL especially when AIL, had initiated the litigation for the purpose of getting possession of the property which was sought to be sold under the agreement dated 23rd December, 1977. In addition to the reasons recorded by the Tribunal for considering the expenditure as revenue expenditure, in our opinion, as opined by the Hon'ble Supreme court in the case of DALMIA JAIN AND CO. LTD. Vs. COMMISSIONER OF INCOME-TAX, BIHAR AND OTHERS (1971) 81 I.T.R. 754, the expenditure incurred by the assessee can be treated only as revenue expenditure. It has been observed by the Hon'ble Supreme Court in the case of DALMIA JAIN AND CO. LTD (supra) that when a suit is resisted by an assessee so as to protect its business and if the proceedings are not initiated by the assessee but when the assessee makes an effort to defend the claim

against it, the expenditure incurred for litigating cannot be treated as capital expenditure and that would be exclusively for the purpose of the business. Looking to the said position, in our opinion, the Tribunal was justified in coming to the conclusion that the expenditure incurred by the assessee was in the nature of revenue expenditure as held by the Hon'ble Supreme Court in the case of DALMIA JAIN AND CO. LTD (Supra). If the expenditure had been incurred by the assessee for the purpose of creating, curing or completing the assessee's title to the capital, then the expenditure incurred would have been considered as capital expenditure. Looking to the facts of the case, it is clear that the expenditure incurred by the assessee was not for the purpose of creating, curing or completing the assesses title to the property in question.

18. For the reasons stated hereinabove and looking to the law laid down by the Hon'ble Supreme Court in the cases referred to hereinabove, we are of the view that the Tribunal had come to a right conclusion by treating the expenditure as revenue expenditure.

In the circumstances, we answer the second question in the affirmative i.e. in favour of the assessee and against the revenue. The reference is answered accordingly with no order as to costs.

(A.R. DAVE,J.)

(D.A. MEHTA,J.)

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